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Item 16. Reserved

Item 16A. Audit Committee Financial Expert

Our board of directors has determined that Daniel Lebègue is an "audit committee financial expert" and that he is independent under the applicable rules promulgated by the Securities and Exchange Commission and The New York Stock Exchange.

Item 16B. Code of Ethics

On February 4, 2004, our board of directors adopted a Code of Ethics for Senior Financial Officers that applies to our Chief Executive Officer, President, Chief Operating Officer, Chief Financial Officer and corporate controller. A copy of our Code of Ethics for Senior Financial Officers has been posted on our Internet website, http://www.alcatel-lucent.com. This Code of Ethics is in addition to our Statement of Business Principles which also applies to our senior financial officers (see Item 6 — "Directors, Senior Management and Employees — Statement of Business Principles, Ethics Committee, Code of Ethics and Chief Compliance Officer").

Item 16C. Principal Accounting Fees and Services

Fees and Services

Under French law, we are required to have two auditors, and we have appointed Ernst & Young et Autres (Ernst & Young) and Deloitte & Associés (Deloitte Touche Tohmatsu) to act in that capacity.

The table below summarizes the audit fees paid by us and our consolidated subsidiaries during each of 2006 and 2005. Regarding our subsidiaries in the space business that are consolidated using proportionate consolidation, fees are taken into account only for the percentage of interests held in these companies.

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Alcatel-Lucent (in thousands of euros, other than %)	2006				2005			
	Deloitte & Associés (Deloitte Touche Tohmatsu)		Ernst & Young et Autres (Ernst & Young)		Deloitte & Associés (Deloitte Touche Tohmatsu)		Ernst & Young et Autres (Ernst & Young)	
	Amount	%	Amount	%	Amount	%	Amount	%
Audit Fees [1]								
Audit Fees	€10,517	90.0%	€7,608	87.8%	€6,875	87.3%	€4,454	88.4%
Audit-Related Fees [2]	1,002	8.5%	753	8.7%	689	8.8%	525	10.4%
Subtotal	**11,519**	**98.5%**	**8,361**	**96.5%**	**7,564**	**96.1%**	**4,979**	**98.8%**
Other Services								
Tax Fees [3]	172	1.5%	301	3.5%	303	3.8%	35	0.7%
All Other Fees [4]	–	0.0%	–	0.0%	7	0.1%	26	0.5%
Subtotal	**172**	**1.5%**	**301**	**3.5%**	**310**	**3.9%**	**61**	**1.2%**
TOTAL	**11,691**	**100.0%**	**8,662**	**100.0%**	**7,874**	**100.0%**	**5,040**	**100.0%**

(1) *"Audit fees" are fees related to (a) statutory audits using applicable sets of accounting standards especially following the business combination with Lucent in 2006, (b) extensive work related to the testing in 2006 of internal controls over financial reporting and the attestation required by Section 404 of the Sarbanes-Oxley Act, (c) audits of the implementation of IFRS in 2005, (d) services associated with AMF and SEC reports and registration statements and (e) accounting or disclosure treatment consultations.*

(2) *"Audit-related fees" are fees generally related to (a) due diligence investigations, primary the business combination with Lucent in 2006, (b) audits of combined financial statements prepared for purposes of the contemplated disposal of certain of our activities (disposal of assets to Thales initiated in 2006) or of combined financial statements of companies that we acquired, (c) other assignments relating to the change over to IFRS in 2005, (d) planning efforts in 2005 related to the review of our internal controls over financial reporting pursuant to Section 404 of the Sarbanes-Oxley Act and (e) the review of internal accounting functions and procedures.*

(3) *"Tax fees" are fees for professional services rendered by our Auditors for tax compliance, tax advice on actual or contemplated transactions, tax consulting associated with international transfer prices and employee tax services.*

(4) *"All other fees" are principally fees related to training and support services.*

Audit and finance committee's pre-approval policies and procedures

Following the business combination with Lucent, our board of directors created the audit and finance committee to replace the then-existing audit committee. The audit and finance committee of our board of directors chooses and engages our independent auditors to audit our financial statements, subject to the approval of our shareholders.

According to the audit and non audit pre-approval policy implemented in 2003 by historical Alcatel's audit committee and confirmed in 2007 by our audit and finance committee, the audit and finance committee gives its approval before engaging our auditors to provide any other audit or permitted non-audit services to us or our subsidiaries. This policy, which is designed to assure that such engagements do not impair the independence of our auditors, requires the audit and finance committee to pre-approve various audit and non-audit services that may be performed by our auditors. In addition, the audit and finance committee limited the aggregate amount of fees our auditors could receive under the pre-approval policy during 2006 for non-audit services in certain categories; fees in excess of such aggregate amount require specific approval. During 2006, approximately 6.1% of tax fees (0% of audit-related and other fees) were neither pre-approved nor specifically approved by the audit and finance committee.

On a quarterly basis, we inform the audit and finance committee of the pre-approved services actually provided by our auditors. Services of a type that are not pre-approved by the audit and finance committee require specific pre-approval by the audit and finance committee's Chairman on a case-by-case basis. The chairman of our audit and finance committee is not permitted to approve any engagement of our auditors if the services to be performed either fall into a category of services that are not permitted by applicable law or the services would be inconsistent with maintaining the auditors' independence.

For information purposes

The following table summarizes fees for professional audit services rendered by PricewaterhouseCoopers for the audits of Lucent's financials statements for the years ended September 30, 2006 and September 30, 2005 and fees billed to Lucent by PricewaterhouseCoopers for other services during fiscal year 2006 and 2005.

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Lucent *(in thousands of euros, other than %)*	PricewaterhouseCoopers 2006 Amount	%	2005 Amount	%
Audit Fees (1)	€ 11,925	84.4%	€ 16,890	84.8%
Audit-Related Fees (2)	1,833	13.0%	1,534	7.7%
Total Audit and Audit-Related Fees	13,758	97.4%	18,424	92.5%
Tax fees (3)				
International Subsidiaries, Tax Return Preparation & Consultation	227	1.6%	426	2.2%
Federal, State and Local Tax	–	0.0%	16	0.1%
Pension & Employee Benefits Services	136	1.0%	560	2.8%
Expatriate Tax Services	3	0.0%	484	2.4%
Total Tax Fees	366	2.6%	1,486	7.5%
All Other Fees	–	0.0%	–	0.0%
TOTAL	**14,124**	**100.0%**	**19,910**	**100.0%**

(1) "Audit fees" are fees related to (a) the audit of consolidated financial statements, (b) services related to Securities Act and Securities Exchange Act filings with the SEC and (c) audits of statutory accounts and related regulatory filings. The decrease in the audit fees for 2006 is due to synergies linked to an integrated audit between statutory accounts, testing of internal controls over financial reporting and attestation required by Section 404 of the Sarbanes-Oxley Act of 2002.

(2) "Audit-related fees" are fees for assurance and related services that are reasonably related to the performance of the audit or review of Lucent's consolidated financial statements. The services in this category include audits of Lucent's employee benefits plans, accounting consultation and due diligence in connection with acquisitions or dispositions.

(3) "Tax fees" are fees for preparation and review of tax returns for international subsidiaries, filings and related services for pension and employee benefits plans, expatriate tax services, and sales and use of tax advisory and recovery services.

Item 16D. Exemptions from the Listing Standards for Audit Committee

Not Applicable.

Item 16E. Purchases of Equity Securities by the Issuer and Affiliated Purchasers

At our annual meeting of shareholders held on September 7, 2006, our shareholders approved a resolution authorizing us, prior to the annual shareholders' meeting to be held in 2007 and at the discretion of our board of directors, to purchase our shares and to hold up to 10% of our share capital. This resolution superseded a similar resolution approved by our shareholders at the annual shareholders' meeting held in 2005.

On December 14, 2006, one of our subsidiaries purchased 910,429 of our ordinary shares at a net price of U.S.$14.113 per share.

As of December 31, 2006, we held directly 25,343,255 of our ordinary shares, and our subsidiaries held a total of 33,406,365 of our ordinary shares.

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Part 3

Item 17. Financial Statements

See Item 18.

Item 18. Financial Statements

The following consolidated financial statements of Alcatel-Lucent, together with the report of Deloitte & Associés and Ernst & Young et Autres for the year ended December 31, 2006 and the report of Deloitte & Associés for the years ended December 31, 2004 and 2005 are filed as part of this annual report.

All schedules have been omitted since they are not required under the applicable instructions or the substance of the required information is shown in the financial statements.

Item 19. Exhibits

1.1 *Statuts* (Articles of Association and By-Laws) of Alcatel-Lucent (English translation) (incorporated by reference to our Post-effective Amendment No.2 on Form S-8 to our Registration Statement on Form F-4, filed November 30, 2006).
2.1 Form of Amended and Restated Deposit Agreement, as further amended and restated as of November 16, 2006, among Alcatel-Lucent, The Bank of New York, as Depositary, and the holders from time to time of the ADSs issued thereunder, including the form of ADR (incorporated by reference to Exhibit A to Alcatel-Lucent's Registration Statement on Form F-6) (File No. 333-138770).
4. Agreement and Plan of Merger, dated April 2, 2006, among Lucent Technologies Inc., Alcatel and Aura Merger Sub, Inc. (incorporated by reference to Exhibit 2.1 to Lucent's Form 8-K dated November 20, 2006).
8. List of subsidiaries (see Note 36 to our consolidated financial statements included elsewhere herein).
10.1 Consent of Independent Registered Public Accounting Firm -- Deloitte & Associés.
10.2 Consent of Independent Registered Public Accounting Firms – Ernst & Young et Autres.
12.1 Certification of the Chief Executive Officer pursuant to §302 of the Sarbanes-Oxley Act of 2002.
12.2 Certification of the Chief Financial Officer pursuant to §302 of the Sarbanes-Oxley Act of 2002.
13.1 Certification of the Chief Executive Officer pursuant to 18 U.S.C. Section 1350.
13.2 Certification of the Chief Financial Officer pursuant to 18 U.S.C. Section 1350.

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15.1 Subordinated Guaranty dated March 27, 2007 executed by Lucent in favor of the holders of Alcatel's 4.375% Bonds due2009 and the Agent therefore.
15.2 Subordinated Guaranty dated March 27, 2007 executed by Lucent in favor of the holders of Alcatel's 4.750% Convertible and/or Exchangeable Bonds due 2011 and the Agent therefore.
15.3 Subordinated Guaranty dated March 27, 2007 executed by Lucent Technologies in favor of the holders of Alcatel's 6.375% Notes due 2014 and the Agent therefore.

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Signature

The registrant hereby certifies that it meets all of the requirements for filing on Form 20–F and that it has duly caused and authorized the undersigned to sign this annual report on its behalf.

ALCATEL–LUCENT

By:	/s/ Jean–Pascal Beaufret
Name:	Jean–Pascal Beaufret
Title:	Chief Financial Officer

April 6, 2007

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The financial statements are presented in accordance with International Financial Reporting Standards (IFRS)

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Alcatel–Lucent and Subsidiaries
Report of Independent Registered Public Accounting Firms

To the Shareholders and the Board of Directors of Alcatel–Lucent:

We have audited the accompanying consolidated balance sheet of Alcatel–Lucent and subsidiaries (the "Group") as of December 31, 2006, and the related consolidated statements of income, changes in shareholders' equity, and cash flows for the year ended December 31, 2006 (all expressed in millions of euros). These consolidated financial statements are the responsibility of Alcatel–Lucent's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, such consolidated financial statements present fairly, in all material respects, the financial position of Alcatel–Lucent and subsidiaries at December 31, 2006, and the consolidated results of their operations and their cash flows for the year ended December 31, 2006, in conformity with International Financial Reporting Standards ("IFRS") as adopted by the European Union.

IFRS as adopted by the European Union vary in certain significant respects from accounting principles generally accepted in the United States of America. The application of the latter would have affected the determination of net loss for the year ended December 31, 2006 and the determination of equity and financial position at December 31, 2006, to the extent summarized in Notes 38 to 41.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the effectiveness of he Group's internal control over financial reporting as of December 31, 2006, based on the criteria established in *Internal Control — Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission and our report dated April 6, 2007 expressed an unqualified opinion thereon.

/s/ Deloitte & Associés

/s/ Ernst & Young et Autres
Represented by Jean–Yves Jegourel

Neuilly–sur–Seine, France
April 6, 2007

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Alcatel and Subsidiaries
Report of Independent Registered Public Accounting Firm

To the Shareholders and the Board of Directors of Alcatel:

We have audited the accompanying consolidated balance sheets of Alcatel and subsidiaries (the "Group") as of December 31, 2005 and 2004, and the related consolidated statements of income, changes in equity, and cash flows for each of the two years in the period ended December 31, 2005 (all expressed in euros). These consolidated financial statements are the responsibility of the Group's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. The Group is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances but not for the purpose of expressing an opinion on the effectiveness of the Group's internal control over financial reporting. Accordingly, we express no such opinion. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, such consolidated financial statements present fairly, in all material respects, the financial position of Alcatel and its subsidiaries as of December 31, 2005 and 2004, and the results of their operations and their cash flows for each of the two years in the period ended December 31, 2005, in conformity with International Financial Reporting Standards ("IFRS") as adopted by the European Union.

IFRS as adopted by the European Union vary in certain significant respects from accounting principles generally accepted in the United States of America. The application of the latter would have affected the determination of net income for each of the two years in the period ended December 31, 2005 and the determination of equity and financial position at December 31, 2005 and 2004, to the extent summarized in Notes 39 to 42.

/s/ Deloitte & Associés
Neuilly–sur–Seine, France
March 30, 2006

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Consolidated income statements

(in millions except per share information)	Note	2006 [1]	2006	2005	2004
Revenues	(4) & (5)	$16,209	€12,282	€11,219	10,263
Cost of sales [2]	(23e)	(10,837)	(8,212)	(7,085)	(6,169)
Gross profit		**5,371**	**4,070**	**4,134**	**4,094**
Administrative and selling expenses [2]	(23e)	(2,521)	(1,910)	(1,815)	(1,771)
Research and development costs [2]	(6) & (23e)	(1,935)	(1,466)	(1,298)	(1,320)
Income (loss) from operating activities before restructuring costs, impairment of intangible assets and gain/(loss) on disposal of consolidated entities	**(4)**	**916**	**694**	**1,021**	**1,003**
Restructuring costs	(27)	(933)	(707)	(79)	(313)
Impairment of intangible assets	(7)	(186)	(141)	-	(88)
Gain/(loss) on disposal of consolidated entities		20	15	129	-
Income (loss) from operating activities		**(183)**	**(139)**	**1,071**	**602**
Financial interest on gross financial debt		*(318)*	*(241)*	*(215)*	*(211)*
Financial interest on cash and cash equivalents		*189*	*143*	*122*	*103*
Finance costs	(8)	(129)	(98)	(93)	(108)
Other financial income (loss)	(8)	(148)	(112)	43	32
Share in net income (losses) of equity affiliates	(16)	29	22	(14)	(61)
Income (loss) before tax, related reduction of goodwill and discontinued operations		**(432)**	**(327)**	**1,007**	**465**
Reduction of goodwill related to realized unrecognized tax loss carry forwards	(9)	(7)	(5)	-	-
Income tax expense	(9)	55	42	(146)	(34)
Income (loss) from continuing operations		**(383)**	**(290)**	**861**	**431**
Income (loss) from discontinued operations	(10)	210	159	110	214
NET INCOME (LOSS)		**$(173)**	**€(131)**	**€971**	**€645**
Attributable to:					
• **Equity holders of the parent**		(232)	(176)	930	576
• Minority interests		59	45	41	69
Net income (loss) attributable to the equity holders of the parent per share *(in euros)*					
• Basic earnings per share	(11)	(0.16)	(0.12)	0.68	0.43
• Diluted earnings per share	(11)	(0.16)	(0.12)	0.68	0.42
Net income (loss) (before discontinued operations) attributable to the equity holders of the parent per share *(in euros)*					
• Basic earnings per share		(0.30)	(0.23)	0.60	0.27
• Diluted earnings per share		(0.30)	(0.23)	0.60	0.26
Net income (loss) of discontinued operations per share *(in euros)*					
• Basic earnings per share		0.15	0.11	0.08	0.16
• Diluted earnings per share		0.15	0.11	0.08	0.16

(1) Translation of amounts from € into $ has been made merely for the convenience of the reader at the Noon Buying Rate of €1 = $1.3197 on December 31, 2006.
(2) Breakdown of share-based payments between cost of sales, administrative and selling expenses and research & development costs is provided in Note 23e.

The accompanying Notes are an integral part of these consolidated financial statements.

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Consolidated balance sheets at December 31

Assets

(in millions)	Note	2006 [1]	2006	2005	2004
Goodwill, net	*(12)*	$14,486	€10,977	€3,772	€3,774
Intangible assets, net	*(13)*	7,056	5,347	819	705
Goodwill and intangible assets, net		**21,542**	**16,324**	**4,591**	**4,479**
Property, plant and equipment, net	*(14)*	2,674	2,026	1,111	1,095
Share in net assets of equity affiliates	*(16)*	900	682	606	604
Other non-current financial assets, net	*(17)*	1,060	803	306	554
Deferred tax assets	*(9)*	2,233	1,692	1,768	1,638
Prepaid pension costs	*(25)*	3,608	2,734	294	287
Marketable securities, net	*(26)*	920	697	-	-
Other non-current assets	*(21)*	268	203	468	332
Total non-current assets		**33,205**	**25,161**	**9,144**	**8,989**
Inventories and work in progress, net	*(18) & (19)*	**2,981**	**2,259**	**1,438**	**1,273**
Amounts due from customers on construction contracts	*(18)*	812	615	917	729
Trade receivables and related accounts, net	*(18) & (20)*	5,116	3,877	3,420	2,693
Advances and progress payments	*(18)*	115	87	124	90
Other current assets	*(21)*	1,328	1,006	827	1,418
Assets held for sale	*(10)*	2,794	2,117	50	196
Current income taxes		338	256	45	78
Marketable securities, net	*(17) & (26)*	1,643	1,245	640	552
Cash and cash equivalents	*(26)*	6,267	4,749	4,510	4,611
Total current assets		**21,394**	**16,211**	**11,971**	**11,640**
Total assets		**$54,599**	**€41,372**	**€21,115**	**€20,629**

(1) Translation of amounts from € into $ has been made merely for the convenience of the reader at the Noon Buying Rate of €1 = $1.3197 on December 31, 2006.

The accompanying Notes are an integral part of these consolidated financial statements.

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Liabilities and shareholders' equity

(in millions)	Note	2006 (1)	2006	2005	2004
Capital stock (€2 nominal value: 2,309,679,141 ordinary shares issued at December 31, 2006, 1,428,541,640 ordinary shares issued at December 31, 2005 and 1,305,455,461 ordinary shares issued and 120,780,519 shares to be issued related to Orane at December 31, 2004)	*(23)*	$6,096	€4,619	€2,857	2,852
Additional paid-in capital		21,700	16,443	8,308	8,226
Less treasury stock at cost		(2,075)	(1,572)	(1,575)	(1,607)
Retained earnings, fair value and other reserves		(4,891)	(3,706)	(4,467)	(4,951)
Cumulative translation adjustments		(152)	(115)	174	(183)
Net income (loss) – attributable to the equity holders of the parent	*(11) & (22)*	(232)	(176)	930	576
Shareholders' equity – attributable to the equity holders of the parent	*(23)*	**20,446**	**15,493**	**6,227**	**4,913**
Minority interests	*(23)*	**657**	**498**	**477**	**373**
Total shareholders' equity	*(23) & (24)*	**21,103**	**15,991**	**6,704**	**5,286**
Pensions, retirement indemnities and other post-retirement benefits	*(25)*	7,035	5,331	1,468	1,466
Bonds and notes issued, long-term	*(24) & (26)*	6,468	4,901	2,393	3,089
Other long-term debt	*(26)*	194	147	359	402
Deferred tax liabilities	*(9)*	3,331	2,524	162	132
Other non-current liabilities	*(21)*	400	303	295	201
Total non-current liabilities		**17,428**	**13,206**	**4,677**	**5,290**
Provisions	*(27)*	3,076	2,331	1,621	2,049
Current portion of long-term debt	*(26)*	1,532	1,161	1,046	1,115
Customers' deposits and advances	*(18) & (29)*	1,027	778	1,144	973
Amounts due to customers on construction contracts	*(18)*	360	273	138	133
Trade payables and related accounts	*(18)*	5,308	4,022	3,755	3,350
Liabilities related to disposal groups held for sale	*(10)*	2,119	1,606	-	97
Current income tax liabilities		87	66	99	179
Other current liabilities	*(21)*	2,558	1,938	1,931	2,157
Total current liabilities		**16,067**	**12,175**	**9,734**	**10,053**
Total liabilities and shareholders' equity		**$54,599**	**€41,372**	**€21,115**	**€20,629**

(1) Translation of amounts from € into $has been made merely for the convenience of the reader at the Noon Buying Rate of €1 = $1.3197 on December 31, 2006.

The accompanying Notes are an integral part of these consolidated financial statements.

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Consolidated statements of cash flows

(millions)	2006 [1]	2006	2005	2004
Cash flows from operating activities				
Net income (loss) – attributable to the equity holders of the parent	$(232)	€(176)	€930	€576
Minority interests	59	45	41	69
Adjustments	1,399	1,060	(89)	(67)
Net cash provided (used) by operating activities before changes in working capital, interest and taxes	**1,226**	**929**	**882**	**578**
Net change in current assets and liabilities (excluding financing):				
• Decrease (increase) in inventories and work in progress	(153)	(116)	(41)	(114)
• Decrease (increase) in trade receivables and related accounts	(181)	(137)	(519)	(184)
• Decrease (increase) in advances and progress payments	(7)	(5)	(35)	3
• Increase (decrease) in trade payables and related accounts	302	229	219	(29)
• Increase (decrease) in customers' deposits and advances	(132)	(100)	84	27
• Decrease (increase) in vendor financing loans [2]	58	44	-	-
• Other current assets and liabilities	(428)	(324)	58	(178)
Cash provided (used) by operating activities before interest and taxes	**686**	**520**	**648**	**103**
• Interest received	144	109	113	111
• Interest paid	(273)	(207)	(136)	(160)
• Taxes (paid)/received	(94)	(71)	(15)	23
Net cash provided (used) by operating activities	**463**	**351**	**610**	**77**
Cash flows from investing activities:				
Proceeds from disposal of tangible and intangible assets	333	252	136	217
Capital expenditures	(903)	(684)	(593)	(528)
Of which impact of capitalization of development costs	*(509)*	*(386)*	*(341)*	*(314)*
Decrease (increase) in loans and other non-current financial assets [2]	-	-	110	422
Cash expenditures for acquisition of consolidated and non-consolidated companies	(560)	(424)	(107)	(116)
Cash and cash equivalents from consolidated companies acquired	1,844	1,397 [3]	22	3
Cash proceeds from sale of previously consolidated and non-consolidated companies	100	76	285	64
(Increase) in marketable securities	190	144	(30)	(265)
Net cash provided (used) by investing activities	**1,004**	**761**	**(177)**	**(203)**
Cash flows from financing activities:				
Issuance/(repayment) of short-term debt	15	11	160	(663)
Issuance of long-term debt	-	-	-	462
Repayment/repurchase of long-term debt	(681)	(516)	(805)	(983)
Proceeds from issuance of shares	25	19	13	12
Proceeds from disposal/(acquisition) of treasury stock	8	6	5	-
Dividends paid	(289)	(219)	(26)	(9)
Net cash provided (used) by financing activities	**(922)**	**(699)**	**(653)**	**(1,181)**
Cash provided (used) by operating activities of discontinued operations	227	172	220	(266)
Cash provided (used) by investing activities of discontinued operations	(32)	(24)	10	299
Cash provided (used) by financing activities of discontinued operations	(210)	(159)	(235)	(100)

Net effect of exchange rate changes	(55)	(42)	124	(50)
Net increase (decrease) in cash and cash equivalents	**475**	**360**	**(101)**	**(1,424)**
Cash and cash equivalents at beginning of period / year	5,952	4,510	4,611	6,035
Cash and cash equivalents at end of period / year	6,267	4,749 (4)	€4,510	€4,611
Cash and cash equivalents at end of period / year classified as assets held for sale	**160**	**121**		

(1) Translation of amounts from € into $has been made merely for the convenience of the reader at the Noon Buying Rate of €1 = $1.3197 on December 31, 2006.
(2) Refer to Note 1v.
(3) Of which cash and cash equivalents held by Lucent Technologies at acquisition date for an amount of €1,391 million.
(4) This amount includes €622 million of cash and cash equivalents held in countries subject to exchange control restrictions. Such restrictions can limit the use of such cash and cash equivalents by other group subsidiaries.

The accompanying Notes are an integral part of these consolidated financial statements.

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Consolidated statements of recognized income and expense

(in millions of euros)	2006	2005	2004
Financial assets available for sale			
Valuation gains/losses taken to equity	*36*	*(13)*	*32*
Transferred to profit or loss on sale	*–*	*(56)*	*–*
Cumulative translation adjustments	(323)	429	(217)
Cash flow hedging	(4)	2	–
Actuarial gains (losses)	–	–	–
Tax on items recognized directly in equity	–	–	–
Other adjustments	8	18	–
Net gains (losses) recognized in equity	**(283)**	**380**	**(185)**
Net income (loss) for the period	(131)	971	645
Total recognized profits (losses) for the period	**(414)**	**1,351**	**460**
Attributable to:			
• **Equity holders of the parent**	**(425)**	**1,238**	**425**
• Minority interests	11	113	35

The accompanying Notes are an integral part of these consolidated financial statements.

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Consolidated statements of changes in shareholders' equity

(in millions of euros except for number of shares outstanding)	Number of shares	Capital stock	Additional paid-in capital	Retained earnings (1)	Changes in fair value and other reserves	Treasury stock	Cumulative translation adjustments	Net income (loss)	Total attributable to the equity holders of the parent	Minority interests	Total
Balance at January 1, 2004	1,342,622,184	2,810	7,966	(4,958)	50	(1,730)	-	-	4,138	388	4,526
Total recognized profit (loss) for 2004					32		(183)	576	425	35	460
Acquisition of Spatial Wireless	17,783,297	36	176						212		212
Other capital increases	3,258,280	6	20						26		26
Deferred share-based payments			60						60		60
Net change in treasury stock of shares owned by consolidated subsidiaries	2,310,066			(88)		123			35		35
Other adjustments			4	13					17	(50)	(33)
Balance at December 31, 2004 before appropriation	1,365,973,827	2,852	8,226	(5,033)	82	(1,607)	(183)	576	4,913	373	5,286
Appropriation of net income (loss)				576				(576)	-	-	-
Balance at December 31, 2004 after appropriation	1,365,973,827	2,852	8,226	(4,457)	82	(1,607)	(183)	-	4,913	373	5,286
Total recognized profit (loss) for 2005				18	(67)		357	930	1,238	113	1,351
Capital increases	2,305,660	5	13						18		18
Deferred share-based payments			69						69		69
Net change in treasury stock of shares owned by consolidated subsidiaries	1,341,444			(37)		32			(5)		(5)
Other adjustments				(6)					(6)	(9)	(15)
December 31, 2005 before appropriation	1,369,620,931	2,857	8,308	(4,482)	15	(1,575)	174	930	6,227	477	6,704
Proposed appropriation of net income (loss)				930				(930)			
Balance at December 31, 2005 after appropriation	1,369,620,931	2,857	8,308	(3,552)	15	(1,575)	174	-	6,227	477	6,704
Total recognized profit (loss) for 2006				8	32		(289)	(176)	(425)	11	(414)
Acquisition of Lucent Technologies (2)	878,139,615	1,756	7,166						8,922		8,922
Other capital increases	2,997,886	6	14						20		20
Equity component of Lucent's convertible debentures (2)			761						761		761
Lucent's warrants (2)			35						35		35
Lucent's outstanding stock options (2)			96						96		96
Deferred share-based payments			63						63		63
Net change in treasury stock owned by consolidated subsidiaries	180,718			(7)		3			(4)		(4)
Dividends				(219)					(219)		(219)
Other adjustments				17					17	10	27
Balance at December 31, 2006 before appropriation	2,250,939,150	4,619	16,443	(3,753)	47	(1,572)	(115)	(176)	15,493	498	15,991
Proposed appropriation of net income (loss)	-			(546)				176	(370)	-	(370)
Balance at December 31, 2006 after appropriation	2,250,939,150	4,619	16,443	(4,299)	47	(1,572)	(115)	-	15,123	498	15,621

(1) Fair value changes relating to marketable securities at fair value through profit or loss were recognized in the income statement in previous accounting periods and appear in retained earnings as a positive amount of €20 million at December 31, 2006. Starting as of January 1, 2006, these changes are directly recognized in shareholders' equity following the revised designation of these marketable securities as financial assets available for sale (see Note 1e).
(2) For more details on the acquisition of Lucent, please refer to Note 3.

The accompanying Notes are an integral part of these consolidated financial statements.

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Notes to consolidated financial statements

Alcatel-Lucent (formerly called Alcatel) is a French public limited liability company that is subject to the French Commercial Code and to all the legal requirements governing commercial companies in France. On November 30, 2006, historical Alcatel completed a business combination with Lucent Technologies, Inc. ("Lucent") and as a result became a wholly-owned subsidiary of Alcatel. Following the transaction historical Alcatel changed its name to Alcatel-Lucent. Alcatel-Lucent was incorporated on June 18, 1898 and will be dissolved on June 30, 2086, except if dissolved earlier or except if its life is prolonged. Alcatel-Lucent's headquarters are situated at 54, rue La Boétie, 75008 Paris, France. Alcatel-Lucent is listed principally on the Paris and New York stock exchanges.

The consolidated financial statements reflect the results and financial position of Alcatel-Lucent and its subsidiaries (the "Group") as well as its investments in associates ("equity affiliates") and joint ventures. They are presented in euros rounded to the nearest million.

The Group develops and integrates technologies, applications and services to offer innovative global communications solutions.

On February 8, 2007, the Board of Directors authorized for issue the consolidated financial statements at December 31, 2006. The consolidated financial statements will only be final once approved at the Annual Shareholders' Meeting.

Note 1 – Summary of accounting policies

Due to the listing of Alcatel-Lucent's securities on the Euronext Paris and in accordance with the European Union's regulation No. 1606/2002 of July 19, 2002, the 2006 consolidated financial statements of the Group are prepared in accordance with IFRSs (International Financial Reporting Standards) as of December 31, 2006, as adopted by the European Union as of the date when our Board of Directors authorized the consolidated financial statements for issue. IFRS include the standards approved by the International Accounting Standards Board ("IASB"), that is, IFRSs, International Accounting Standards ("IASs") and the accounting interpretations issued by the International Financial Reporting Interpretations Committee ("IFRIC") or the former Standing Interpretations Committee ("SIC").

Between 1999 and 2004, the consolidated financial statements of the Group were prepared in accordance with French generally accepted accounting principles ("French GAAP") in compliance with the "Principles and accounting methodology relative to consolidated financial statements" regulation No. 99-02 of the *"Comité de la réglementation comptable"* approved by the decree dated June 22, 1999.

As a first-time adopter of IFRS at December 31, 2005, Alcatel followed IFRS 1 regulations governing the first-time adoption of IFRSs by companies. Reconciliation schedules of the 2004 consolidated net income, consolidated statement of cash flows and consolidated shareholders' equity at both January 1, 2004 and December 31, 2004 between IFRSs and those prepared previously in accordance with French GAAP were included in the 2005 consolidated financial statement disclosure notes. At the transition date (January 1, 2004), the following options were selected:

- business combinations that were completed before the transition date were not restated;
- the accumulated total of translation adjustments at the transition date were deemed to be zero;
- the accumulated unrecognized actuarial gains and losses at the transition date relating to pension and retirement obligations and other employee and post-employment benefit obligations were recorded in shareholders' equity;
- property, plant and equipment was not revalued;
- only stock options issued after November 7, 2002 and not fully vested at January 1, 2005 were accounted for in accordance with IFRS 2;
- all the Group's subsidiaries, equity affiliates and joint ventures adopted IFRSs at the same date as the parent company;
- all the requirements of IAS 32 "Financial Instruments: Disclosure and Presentation", IAS 39 "Financial Instruments: Recognition and Measurement" and IFRS 5 "Non-current Assets Held for Sale and Discontinued Operations" have been applied since January 1, 2004;
- early application, as from January 1, 2004, of interpretations IFRIC 4 "Determining whether an Arrangement contains a Lease" and IFRIC 6 "Liabilities arising from Participating in a Specific Market—Waste Electrical and Electronic Equipment".

All standards and interpretations applied by Alcatel-Lucent in these consolidated financial statements are in compliance with both the European directives and the IFRSs adopted by the European Union.

(a) Basis of preparation

The consolidated financial statements have been prepared under the historical cost convention, with the exception of certain categories of assets and liabilities, in accordance with IFRSs. The categories concerned are detailed in the following notes.

(b) Consolidation methods

Companies over which the Group has control are fully consolidated.

Companies over which the Group has joint control are accounted for using proportionate consolidation.

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Companies over which the Group has a significant influence (investments in "associates" or equity affiliates) are accounted for under the equity method. Significant influence is assumed when the Group's interest in the voting rights is greater than or equal to 20%.

All significant intra-group transactions are eliminated.

(c) Business combinations

Regulations governing first-time adoption: Business combinations that were completed before January 1, 2004, the transition date to IFRSs, were not restated, as permitted by the optional exemption included in IFRS 1. Goodwill was therefore not recognized for business combinations occurring prior to January 1, 2004, which were previously accounted for in accordance with article 215 of Regulation No. 99-02 of the *"Comité de la réglementation comptable"*. According to this regulation, the assets and liabilities of the acquired company are maintained at their carrying value at the date of the acquisition, adjusted for the Group's accounting policies, and the difference between this value and the acquisition cost of the shares is adjusted directly against shareholders' equity.

Business combinations after January 1, 2004: These business combinations are accounted for in accordance with the purchase method. Once control is obtained over a company, its assets, liabilities and contingent liabilities are measured at their fair value at the acquisition date in accordance with IFRS requirements. Any difference between the fair value and the carrying value is accounted for in the respective underlying asset or liability, including both the Group interest and minority interests. Any excess between the purchase price and the Group's share in the fair value of such net assets is recognized as goodwill (see intangible and tangible assets).

If the initial accounting for a business combination cannot be completed before the end of the annual period in which the business combination is effected, the initial accounting shall be completed within twelve months of the acquisition date.

The accounting treatment of deferred taxes related to business combinations is described in Note 1n below.

The accounting treatment of stock options of companies acquired in the context of a business combination is described in Note 1w below.

(d) Translation of financial statements denominated in foreign currencies

The balance sheets of consolidated subsidiaries having a functional currency different from the euro are translated into euros at the closing exchange rate (spot exchange rate at the balance sheet date), and their income statements and cash flow statements are translated at the average exchange rate. The resulting translation adjustments are included in shareholders' equity under the caption "Cumulative translation adjustments".

Goodwill and fair value adjustments arising from the acquisition of a foreign entity are considered as assets and liabilities of that entity. They are therefore expressed in the entity's functional currency and translated using the closing exchange rate.

Regulations governing first-time adoption: In accordance with the option available under IFRS 1, the accumulated total of translation adjustments at the transition date was deemed to be zero. This amount was reversed against retained earnings, leaving the amount of shareholders' equity unchanged. Translation adjustments that predate the IFRS transition will therefore not be included when calculating gains or losses arising from the future disposal of consolidated subsidiaries or equity affiliates existing as of the IFRS transition date.

(e) Translation of foreign currency transactions

Foreign currency transactions are translated at the rate of exchange applicable on the transaction date. At period-end, foreign currency monetary assets and liabilities are translated at the rate of exchange prevailing on that date. The resulting exchange gains or losses are recorded in the income statement in "other financial income (loss)".

Exchange gains or losses on foreign currency financial instruments that represent an economic hedge of a net investment in a foreign subsidiary are reported as translation adjustments in shareholders' equity under the caption "Cumulative translation adjustments" until the disposal of the investment. Refer to Note 1d above for information on the recognition of translation adjustments at the IFRS transition date.

In order for a currency derivative to be eligible for hedge accounting treatment (cash flow hedge or fair value hedge), its hedging role must be defined and documented and it must be seen to be effective for the entirety of its period of use. Fair value hedges allow companies to protect themselves against exposure to changes in fair value of their assets, liabilities or firm commitments. Cash flow hedges allow companies to protect themselves against exposure to changes in future cash flows (for example, revenues generated by the company's assets).

The value used for derivatives is their fair value. Changes in the fair value of derivatives are accounted for as follows:

- For derivatives treated as cash flow hedges, changes in their fair value are accounted for in shareholders' equity and then reclassified to income (cost of sales) when the hedged revenue is accounted for. The ineffective portion is recorded in "other financial income (loss)";
- For derivatives treated as fair value hedges, changes in their fair value are recorded in the income statement where they offset the changes in fair value of the hedged assets, liabilities and firm commitments.

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In addition to derivatives used to hedge firm commitments documented as fair value hedges, from April 1, 2005 onwards, Alcatel–Lucent designates and documents highly probable future streams of revenue with respect to which the Group has entered into hedge transactions. The corresponding derivatives are accounted for in accordance with the requirements governing cash flow hedge accounting.

Foreign exchange derivatives used by Lucent and its affiliates are not considered eligible for hedge accounting treatment, as the derivatives are not designated as hedges for cost/benefit reasons.

Derivatives related to commercial bids are not considered eligible for hedge accounting treatment and are accounted for as trading financial instruments. Changes in fair values of such instruments are included in the income statement in cost of sales (in the business segment "other").

Once a commercial contract is effective, the corresponding firm commitment is hedged with a derivative treated as a fair value hedge. Revenues made pursuant to such a contract are then accounted for, throughout the duration of the contract, using the spot rate prevailing on the date on which the contract was effective, insofar as the exchange rate hedging is effective.

(f) Research and development expenses

In accordance with IAS 38 "Intangible Assets", research and development expenses are recorded as expenses in the year in which they are incurred, except for:

- development costs, which are capitalized as an intangible asset when they strictly comply with the following criteria:
  - the project is clearly defined, and the costs are separately identified and reliably measured,
  - the technical feasibility of the project is demonstrated,
  - the intention exists to finish the project and use or sell the products created during the project,
  - a potential market for the products created during the project exists or their usefulness, in case of internal use, is demonstrated, and
  - adequate resources are available to complete the project.

  These development costs are amortized over the estimated useful life of the projects concerned.

  The amortization of capitalized development costs begins as soon as the product in question is released.

  Specifically for software, useful life is determined as follows:
  - in case of internal use: over its probable service lifetime,
  - in case of external use: according to prospects for sale, rental or other forms of distribution.

  Capitalized software development costs are those incurred during the programming, codification and testing phases. Costs incurred during the design and planning, product definition and product specification stages are accounted for as expenses.

  The amortization of capitalized software costs during a reporting period shall be the greater of the amount computed using (a) the ratio that current gross revenues for a product bear to the total of current and anticipated future gross revenues for that product and (b) the straight–line method over the remaining estimated economic life of the product;
- *customer design engineering costs* (recoverable amounts disbursed under the terms of contracts with customers), which are included in work in progress on construction contracts.

With regard to business combinations, Alcatel–Lucent allocates a portion of the purchase price to in–process research and development projects that may be significant. As part of the process of analyzing these business combinations, Alcatel–Lucent may make the decision to buy technology that has not yet been commercialized rather than develop the technology internally. Decisions of this nature consider existing opportunities for Alcatel–Lucent to stay at the forefront of rapid technological advances in the telecommunications–data networking industry.

The fair value of in–process research and development acquired in business combinations is based on present value calculations of income, an analysis of the project's accomplishments and an evaluation of the overall contribution of the project, and the project's risks.

The revenue projection used to value in–process research and development is based on estimates of relevant market sizes and growth factors, expected trends in technology, and the nature and expected timing of new product introductions by Alcatel–Lucent and its competitors. Future net cash flows from such projects are based on management's estimates of such projects' cost of sales, operating expenses and income taxes.

The value assigned to purchased in–process research and development is also adjusted to reflect the stage of completion, the complexity of the work completed to date, the difficulty of completing the remaining development, costs already incurred, and the projected cost to complete the projects.

Such value is determined by discounting the net cash flows to their present value. The selection of the discount rate is based on Alcatel–Lucent's weighted average cost of capital, adjusted upward to reflect additional risks inherent in the development life cycle.

Capitalized development costs considered as assets (either generated internally and capitalized or reflected in the purchase price of a business combination) are generally amortized over 3 to 10 years.

Impairment tests are carried out, using the methods described in the following paragraph.

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(g) Goodwill, intangible assets and property, plant and equipment

In accordance with IAS 16 "Property, Plant and Equipment" and with IAS 38 "Intangible Assets", only items whose cost can be reliably measured and for which future economic benefits are likely to flow to the Group are recognized as assets.

In accordance with IAS 36 "Impairment of Assets", whenever events or changes in market conditions indicate a risk of impairment of intangible assets and property, plant and equipment, a detailed review is carried out in order to determine whether the net carrying amount of such assets remains lower than their recoverable amount, which is defined as the greater of fair value (less costs to sell) and value in use. Value in use is measured by discounting the expected future cash flows from continuing use of the asset and its ultimate disposal.

In the event that the recoverable value is lower than the net carrying value, the difference between the two amounts is recorded as an impairment loss. Impairment losses for property, plant and equipment or intangible assets with finite useful lives can be reversed if the recoverable value becomes higher than the net carrying value (but not exceeding the loss initially recorded).

Goodwill

Since transition to IFRSs, goodwill is no longer amortized in accordance with IFRS 3 "Business Combinations". Before January 1, 2004, goodwill was amortized using the straight–line method over a period, determined on a case–by–case basis, not exceeding 20 years.

Each goodwill item is tested for impairment annually. It is done during the second quarter of the year. The impairment test methodology is based on a comparison between the recoverable amounts of each of the Group's business divisions (considered as the grouping of cash generating units ("CGU") at which level the impairment test is performed) with the business division's net asset carrying values (including goodwill). In the reporting structure, the Business Divisions are one level below the Business Groups for the Carrier Business Segment and one level below the Business Segment for the two other Business Segments. Such recoverable amounts are mainly determined using discounted cash flows over five years and a discounted residual value. The discount rate used for the annual impairment test was the Group's weighted average cost of capital of 10.8% for 2004 and 9.5% for 2005 and for 2006. These discount rates are after–tax rates applied to after–tax cash flows. The use of such rates results in recoverable values that are identical to those that would be obtained by using, as required by IAS 36, before–tax rates applied to before–tax cash flows. A single discount rate has been used on the basis that risks specific to certain products or markets have been reflected in determining the cash flows. Management believes the assumptions used concerning sales growth and residual values are reasonable and in line with market data available for each business division. Further impairment tests are carried out if events occur indicating a potential impairment. Goodwill impairment losses cannot be reversed.

Equity affiliate goodwill is included with the related investment in "share in net assets of equity affiliates". The requirements of IAS 39 are applied to determine whether any impairment loss must be recognized with respect to the net investment in equity affiliates. The impairment loss is calculated according to IAS 36 requirements.

When the reporting structure is reorganized in a way that changes the composition of one or more business divisions to which goodwill has been allocated, a new impairment test is performed on the goodwill for which underlying business divisions have been changed. Such a reallocation has been made in December 2006 using a relative value approach similar to the one used when an entity disposes of an operation within a Business Division.

Intangible assets

Intangible assets mainly include capitalized development costs and those assets acquired in business combinations, primarily acquired technologies or customer relationships. Intangible assets, other than trade names, are generally amortized on a straight–line basis over a 3 to 10 year period. However, software amortization methods may be adjusted to take into account how the product is marketed. Amortization are accounted for in the income statement under cost of sales, research and development expenses (acquired technology, IPR&D, etc.) or administrative and selling expenses (customer relationships), depending on the designation of the asset. Impairment losses are accounted for in the above mentioned line items or in restructuring costs if part of a restructuring plan or on a specific line item if very material (refer to Note 1p). No intangible assets are considered to have indefinite useful lives other than some trade names. All intangible assets, with the exception of some trade names, are amortized over their estimated useful lives. Trade names could have an indefinite useful life and are therefore not amortized.

Property, plant and equipment

Property, plant and equipment are valued at historical cost for the Group less accumulated depreciation expenses and any impairment losses. Depreciation expense is generally calculated over the following useful lives:

- buildings and building improvements — 5–50 years
- infrastructure and fixtures — 5–20 years
- plant and equipment — 2–10 years

Depreciation expense is determined using the straight–line method.

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Fixed assets acquired through finance lease arrangements or long−term rental arrangements that transfer substantially all the risks and rewards associated with ownership of the asset to the Group (tenant) are capitalized.

Residual value, if considered to be significant, is included when calculating the depreciable amount. Property, plant and equipment are segregated into their separate components if there is a significant difference in their expected useful lives, and depreciated accordingly.

Depreciation and impairment losses are accounted for in the income statement under "cost of sales", "research and development costs" or "administrative and selling expenses", depending on the nature of the asset (see Note 1p).

(h) Non−consolidated investments and other non−current financial assets

In accordance with IAS 39 "Financial Instruments: Recognition and Measurement", investments in non−consolidated companies are classified as available−for−sale and therefore measured at their fair value. The fair value for listed securities is their market price. If a reliable fair value cannot be established, securities are valued at cost. Fair value changes are accounted for directly in shareholders' equity. When objective evidence of impairment of a financial asset exists (for instance, a significant or prolonged decline in the value of an asset), an irreversible impairment loss is recorded. This loss can only be released upon the sale of the securities concerned.

Loans are measured at amortized cost. Loans may suffer impairment losses if there is objective evidence of a loss in value. The impairment represented by the difference between net carrying amount and recoverable value is recognized in the income statement and can be reversed if recoverable value rises in the future.

The portfolio of non−consolidated securities and other financial assets is examined at each quarter−end to detect any objective evidence of impairment. When this is the case, an impairment loss is recorded. Impairment losses on securities accounted for at quarter−ends are irreversible and could only be released upon the sale of the securities concerned.

(i) Inventories and work in progress

Inventories and work in progress are valued at the lower of cost (including indirect production costs where applicable) or net realizable value.

Net realizable value is the estimated sales revenue for a normal period of activity less expected completion and selling costs.

(j) Treasury stock

Treasury shares owned by Alcatel−Lucent or its subsidiaries are valued at their cost price and are deducted from shareholders' equity. Proceeds from the sale of such shares are included directly in shareholders' equity and have no impact on the income statement.

(k) Pension and retirement obligations and other employee and post−employment benefit obligations

Post−employment benefits:

In accordance with the laws and practices of each country where Alcatel−Lucent is established, the Group participates in employee benefit plans.

For defined contribution plans, the Group expenses contributions as and when they are due. As the Group is not liable for any legal or constructive obligations under the plans beyond the contributions paid, no provision is made. Provisions for defined benefit plans and other long−term employee benefits are determined as follows:

- using the Projected Unit Credit Method (with projected final salary), each period of service gives rise to an additional unit of benefit entitlement and each unit is measured separately to calculate the final obligation. Actuarial assumptions such as mortality rates, rates of employee turnover and projection of future salary levels are used to calculate the obligation;
- using the "corridor" method, only actuarial gains and losses in excess of either 10% of the present value of the defined benefit obligation or 10% of the fair value of any plan assets, whichever is greater, are recognized over the expected average remaining working lives of the employees participating in the plan or at 100% in the following year if the participants are no longer working.

The expense resulting from the change in net pension and other post−retirement obligations is recorded in "income (loss) from operating activities before restructuring costs, impairment of intangible assets and gain/(loss) on disposal of consolidated entities" or in "other financial income (loss)" depending upon the nature of the underlying obligation. Generally, the service cost is recognized in the income from operating activities and the interest cost and expected return on plan assets are recognized in the financial result.

Under IFRS, plan assets are limited to the lower of: (i) the value resulting from applying IAS 19—Employee Benefits, and (ii) the net total present value of any available refund from the plan or reduction in future contributions to the plan. As the company plans to use excess pension assets to fund retiree healthcare for formerly represented retirees and has the ability to do so, such use has been analyzed as refund from the related plan. In fact, under section 420 of the Income Revenue Code in the United States of America as amended by the Pension Protection Act of 2006, the company is authorized until 2013 (according to current legislation) to use excess pension assets to fund retiree healthcare plan for formerly represented retirees.

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At this time, the Group is considering whether to adopt the new option provided for in IAS 19 "Employee Benefits—Actuarial Gains and Losses, Group Plans and Disclosures" that allows the full amount of actuarial gains and losses to be recorded outside profit or loss in a statement of recognized income and expense.

Regulations governing first-time adoption: In accordance with the option available under IFRS 1, the accumulated unrecognized actuarial gains and losses at the transition date were recorded in shareholders' equity. The corridor method has been applied starting January 1, 2004.

Certain other post-employment benefits such as life insurance and health insurance (particularly in the United States) or long-service medals (bonuses awarded to employees for long service particularly in French and German companies), are also recognized as provisions, which are determined by means of an actuarial calculation similar to the one used for retirement provisions.

The accounting treatment used for employee stock options is detailed in Note 1w below.

(l) Provisions for restructuring and restructuring costs

Provisions for restructuring costs are made when restructuring programs have been finalized and approved by Group management and have been announced before the balance sheet date of the Group's financial statements, resulting in an obligating event of the Group to third parties. Such costs primarily relate to severance payments, early retirement, costs for notice periods not worked, training costs of terminated employees, costs linked to the closure of facilities or the discontinuance of product lines and any costs arising from plans that materially change the scope of the business undertaken by the Group or the manner in which such business is conducted. Other costs (removal costs, training costs of transferred employees, etc) and write-offs of fixed assets, inventories and work in progress and other assets, directly linked to restructuring measures, are also accounted for in restructuring costs.

The amounts reserved for anticipated severance payments made in the context of restructuring programs are valued at their present value in cases where the settlement date is beyond the normal operating cycle of the company and the time value of money is deemed to be significant. The impact of the passage of time on the present value of the payments is included in other financial income (loss).

(m) Financial debt—Compound financial instruments

Some financial instruments contain both a liability and an equity component. This is the case with the bonds issued by Alcatel in 2003 ("OCEANE—*Obligation Convertible ou Échangeable en Actions Nouvelles ou Existantes*", bonds that can be converted into or exchanged for new or existing shares) and in 2002 ("ORANE—*Obligation Remboursable en Actions Nouvelles ou Existantes*", notes mandatorily redeemable for new or existing shares) or compound financial instruments issued by Lucent prior to the merger in 2006 between Alcatel and Lucent. The different components of compound financial instruments are accounted for in shareholders' equity and in bonds and notes issued according to their classification, as defined in IAS 32 "Financial Instruments: Disclosure and Presentation".

For instruments issued by Alcatel, the component classified as a financial liability was valued on the issuance date at present value (taking into account the credit risk at issuance date) of the future cash flows (including interest and repayment of the nominal value) of a bond with the same characteristics (maturity, cash flows) but without any equity component. The portion included in shareholders' equity results from the difference between the debt issue amount and the financial liability component.

At the merger closing date, the financial liability component of Lucent's convertible bonds was computed at present value as described in the preceding paragraph, taking into account contractual maturities. The difference between the fair value of the convertible debentures and the corresponding financial liability component was accounted for as a component of equity.

(n) Deferred taxation

Deferred taxes are computed in accordance with the liability method for all temporary differences arising between the tax bases of assets and liabilities and their carrying amounts, including the reversal of entries recorded in individual accounts of subsidiaries solely for tax purposes. All amounts resulting from changes in tax rates are recorded in shareholder's equity or in net income (loss) for the year in which the tax rate change is enacted.

Deferred tax assets are recorded in the consolidated balance sheet when it is probable that the tax benefit will be realized in the future. Deferred tax assets and liabilities are not discounted.

To assess the ability of the Group to recover deferred tax assets, the following factors are taken into account:

- existence of deferred tax liabilities that are expected to generate taxable income, or limit tax deductions upon reversal;
- forecasts of future tax results;
- the impact of non-recurring costs included in income or loss in recent years that are not expected to be repeated in the future;
- historical data concerning recent years' tax results; and
- if required, tax planning strategy, such as the planned disposal of undervalued assets.